

**REPORT OF THE AUDIT OF THE
MARTIN COUNTY
SHERIFF'S SETTLEMENT - 2002 TAXES**

**For The Period January 6, 2003
Through May 14, 2003**



**EDWARD B. HATCHETT, JR.
AUDITOR OF PUBLIC ACCOUNTS
www.kyauditor.net**

**144 CAPITOL ANNEX
FRANKFORT, KY 40601
TELEPHONE (502) 564-5841
FACSIMILE (502) 564-2912**



EDWARD B. HATCHETT, JR.
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky

Honorable Paul E. Patton, Governor

Gordon C. Duke, Secretary

Finance and Administration Cabinet

Dana Mayton, Secretary, Revenue Cabinet

Honorable Kelly Callahan, Martin County Judge/Executive

Honorable Garmon Preece, Martin County Sheriff

Members of the Martin County Fiscal Court

The enclosed report prepared by Morgan-Franklin, LLC, Certified Public Accountants, presents the Martin County Sheriff's Settlement - 2002 Taxes.

We engaged Morgan-Franklin, LLC, to perform the financial audit of this statement. We worked closely with the firm during our report review process; Morgan-Franklin, LLC, evaluated the Martin County Sheriff's internal controls and compliance with applicable laws and regulations.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Ed Hatchett".

Edward B. Hatchett, Jr.

Auditor of Public Accounts

Enclosure

EXECUTIVE SUMMARY

**AUDIT EXAMINATION OF THE
MARTIN COUNTY
SHERIFF'S SETTLEMENT - 2002 TAXES**

**For The Period January 6, 2003
Through May 14, 2003**

Morgan-Franklin, LLC, has completed the audit of the Sheriff's Settlement - 2002 Taxes for Martin County Sheriff as of May 14, 2003. We have issued an unqualified opinion on the financial statement taken as a whole. Based upon the audit work performed, the financial statement is presented fairly in all material respects.

Financial Condition:

The Sheriff collected taxes of \$1,317,131 for the districts for 2002 taxes, retaining commissions of \$35,378 to operate the Sheriff's office. The Sheriff distributed taxes of \$1,285,124 to the districts for 2002 Taxes. Taxes of \$2,865 are due to the districts from the Sheriff and refunds of \$4,214 are due to the Sheriff from the taxing districts.

Report Comments:

- The Sheriff Should Have A Written Agreement To Protect Deposits
- The County Sheriff Should Not Transfer Money From The Fee Account To The Tax Account
- Lacks Adequate Segregation Of Duties

Deposits:

The Sheriff's deposits were uninsured and uncollateralized by bank securities or bonds.

CONTENTS

PAGE

INDEPENDENT AUDITOR'S REPORT	1
SHERIFF'S SETTLEMENT - 2002 TAXES	3
NOTES TO FINANCIAL STATEMENTS	5
COMMENTS AND RECOMMENDATIONS	9
REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF THE FINANCIAL STATEMENT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS	12

**Morgan-Franklin, LLC
P.O. Box 428
513 Main Street
West Liberty, Kentucky 41472**

To the People of Kentucky

Honorable Paul E. Patton, Governor

Gordon C. Duke, Secretary

Finance and Administration Cabinet

Dana Mayton, Secretary, Revenue Cabinet

Honorable Kelly Callahan, Martin County Judge/Executive

Honorable Garmon Preece, Martin County Sheriff

Members of the Martin County Fiscal Court

Independent Auditor's Report

We have audited the Martin County Sheriff's Settlement - 2002 Taxes for the period January 6, 2003 through May 14, 2003. This tax settlement is the responsibility of the Martin County Sheriff. Our responsibility is to express an opinion on the financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for Sheriff's Tax Settlements issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the Sheriff's office prepares the financial statement on a prescribed basis of accounting that demonstrates compliance with the modified cash basis and laws of Kentucky, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the accompanying financial statement referred to above presents fairly, in all material respects, the Martin County Sheriff's taxes charged, credited, and paid for the period January 6, 2003, through May 14, 2003, in conformity with the modified cash basis of accounting.

To the People of Kentucky

Honorable Paul E. Patton, Governor

Gordon C. Duke, Secretary

Finance and Administration Cabinet

Dana Mayton, Secretary, Revenue Cabinet

Honorable Kelly Callahan, Martin County Judge/Executive

Honorable Garmon Preece, Martin County Sheriff

Members of the Martin County Fiscal Court

In accordance with Government Auditing Standards, we have also issued our report dated October 6, 2003, on our consideration of the Sheriff's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Based on the results of our audit, we present the accompanying comments and recommendations, included herein, which discusses the following report comments:

- The Sheriff Should Have A Written Agreement To Protect Deposits
- The County Sheriff Should Not Transfer Money From The Fee Account To The Tax Account
- Lacks Adequate Segregation Of Duties

Respectfully submitted,

Morgan - Franklin, LLC

Morgan-Franklin, LLC

Audit fieldwork completed -
October 6, 2003

MARTIN COUNTY
GARMON PREECE, COUNTY SHERIFF
SHERIFF'S SETTLEMENT - 2002 TAXES

For The Period January 6, 2003 Through May 14, 2003

<u>Charges</u>	<u>County Taxes</u>	<u>Special Taxing Districts</u>	<u>School Taxes</u>	<u>State Taxes</u>
Transferred To Incoming Sheriff	\$ 53,947	\$ 63,528	\$ 217,259	\$ 87,089
Omitted Taxes	3,493	3,950	14,842	4,122
Franchise Corporation	46,835	58,748	186,049	
Additional Billings	32,138	642	139,551	38,001
Unmined Coal - 2002 Taxes	73,032	117,240	294,668	85,733
Oil and Gas Property Taxes	6,277	6,987	25,327	7,369
Penalties	2,394	2,813	9,684	5,346
Gross Chargeable to Sheriff	<u>\$ 218,116</u>	<u>\$ 253,908</u>	<u>\$ 887,380</u>	<u>\$ 227,660</u>
<u>Credits</u>				
Exonerations	1,580	1,759	6,376	1,855
Discounts	1,854	2,080	7,673	2,182
Delinquents:				
Real Estate	22,016	25,534	88,830	25,845
Tangible Personal Property	1,097	2,636	4,286	21,985
Intangible Personal Property				37
Unmined Coal - 2002 Taxes	3,677	4,093	14,836	4,317
Uncollected Franchise	4,083	4,794	16,297	
Adjustment		211		
Total Credits	<u>\$ 34,307</u>	<u>\$ 41,107</u>	<u>\$ 138,298</u>	<u>\$ 56,221</u>
Taxes Collected	\$ 183,809	\$ 212,801	\$ 749,082	\$ 171,439
Less: Commissions *	<u>7,812</u>	<u>9,044</u>	<u>11,236</u>	<u>7,286</u>
Taxes Due	\$ 175,997	\$ 203,757	\$ 737,846	\$ 164,153
Taxes Paid	174,753	204,314	743,914	162,143
Refund of School Commissions			(5,415)	
Refunds (Current and Prior Year)	<u>179</u>	<u>328</u>	<u>2,676</u>	<u>210</u>
Due Districts or (Refunds Due Sheriff)		**		
as of Completion of Fieldwork	<u>\$ 1,065</u>	<u>\$ (885)</u>	<u>\$ (3,329)</u>	<u>\$ 1,800</u>

* and ** See Page 4.

The accompanying notes are an integral part of this financial statement.

MARTIN COUNTY
GARMON PREECE, COUNTY SHERIFF
SHERIFF'S SETTLEMENT - 2002 TAXES
For The Period January 6, 2003 Through May 14, 2003
(Continued)

* Commissions:

4.25% on	\$	568,049
1.5% on	\$	749,082

** Special Taxing Districts:

Library District	\$	(855)
Health District		(1,303)
Extension District		1,399
Inez City		<u>(126)</u>
Due Districts or (Refunds Due Sheriff)	\$	<u><u>(885)</u></u>

The accompanying notes are an integral part of this financial statement.

MARTIN COUNTY
NOTES TO FINANCIAL STATEMENTS

For The Period January 6, 2003 Through May 14, 2003

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

The Sheriff's office tax collection duties are limited to acting as an agent for assessed property owners and taxing districts. A fund is used to account for the collection and distribution of taxes. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

B. Basis of Accounting

The financial statement has been prepared on a modified cash basis of accounting. Basis of accounting refers to when charges, credits, and taxes paid are reported in the settlement statement. It relates to the timing of measurements regardless of the measurement focus.

Charges are sources of revenue, which are recognized in the tax period in which they become available and measurable. Credits are reductions of revenue, which are recognized when there is proper authorization. Taxes paid are uses of revenue, which are recognized when distributions are made to the taxing districts and others.

C. Cash and Investments

At the direction of the fiscal court, KRS 66.480 authorizes the Sheriff's office to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

Note 2. Deposits

The Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the Sheriff and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. As of May 14, 2003, the bank balances were fully insured or collateralized at a 100% level with collateral of either pledged securities held by the Sheriff's agent in the Sheriff's name, or provided surety bond which named the Sheriff as beneficiary/obligee on the bond.

MARTIN COUNTY
NOTES TO FINANCIAL STATEMENTS
For The Period January 6, 2003 Through May 14, 2003
(Continued)

Note 2. Deposits (Continued)

However, as of February 19, 2003 and March 14, 2003, the dates of the highest balances at Inez Deposit Bank and Family Bank, respectively, the collateral and FDIC insurance together did not equal or exceed the amount on deposit, leaving a total of \$860,712 of public funds uninsured and unsecured. In addition, the Sheriff did not have a written agreement with the depository institutions securing the Sheriff's interest in the collateral.

The Martin County Sheriff's deposits are categorized below to give an indication of the level of risk assumed by the Sheriff as of February 19, 2003 and March 14, 2003.

	Inez Deposit Bank Balance	Family Bank Balance	Total
FDIC insured	\$ 100,000	\$ 100,000	\$ 200,000
Collateralized with securities held by pledging depository institution in the county official's name	0	0	0
Uncollateralized and uninsured	<u>267,737</u>	<u>592,975</u>	<u>860,712</u>
Total	<u>\$ 367,737</u>	<u>\$ 692,975</u>	<u>\$ 1,060,712</u>

Note 3. Tax Collection Period

A. Property Taxes

The real and personal property tax assessments were levied as of January 1, 2002. Property tax assessments were billed to finance governmental services for the year ended June 30, 2003. Liens are effective when the tax bills become delinquent. The collection period for the property tax assessments was January 15, 2003 through May 14, 2003.

B. Unmined Coal Taxes

The tangible property tax assessments were levied as of January 1, 2002. Property taxes are billed to finance governmental services. Liens are effective when the tax bills become delinquent. The collection period for these assessments was February 14, 2003 through May 14, 2003.

Note 4. Interest Income

The Martin County Sheriff earned \$331 as interest income on taxes. The Sheriff distributed the appropriate amount to the school district as required by statute, and the remainder will be used to operate the Sheriff's office. As of October 6, 2003, the Sheriff owes \$44 in interest to the school district and the Sheriff's tax account is due a refund of \$5 in interest from the fee account.

MARTIN COUNTY
NOTES TO FINANCIAL STATEMENTS
For The Period January 6, 2003 Through May 14, 2003
(Continued)

Note 5. Sheriff's 10% Add-On Fee

The Martin County Sheriff collected \$9,817 of 10% add-on fees allowed by KRS 134.430(3). This amount will be used to operate the Sheriff's office.

Note 6. Advertising Costs And Fees

The Martin County Sheriff collected \$2,780 of advertising costs allowed by KRS 424.330(1) and KRS 134.440(2). The Sheriff distributed the advertising costs to the county as required by statute, and the advertising fees will be used to operate the Sheriff's office. As of October 6, 2003, the Sheriff owes \$2,780 in advertising costs to the county. Subsequent to the audit report date, this amount was paid to the county.

Note 7. Commission Rate On School Taxes

Pursuant to KRS 160.500, school taxes shall be collected by the sheriff for county school districts and by the regular tax collector of the city or special tax collector.... The tax collector shall be entitled to a fee equal to his expense but not less than one and one-half percent and not to exceed the rate of four percent for the collection of school taxes... The Martin County Sheriff has sent a justification to the state providing information to support his claim that the one and one-half percent sheriff commission rate on school taxes for the 2002 tax year does not cover the Sheriff's expenses for collection of the school's taxes. The Sheriff may pursue legal action if this matter cannot be resolved by other means.

THIS PAGE LEFT BLANK INTENTIONALLY

COMMENTS AND RECOMMENDATIONS

MARTIN COUNTY
GARMON PREECE, COUNTY SHERIFF
COMMENTS AND RECOMMENDATIONS

For The Period January 6, 2003 Through May 14, 2003

STATE LAWS AND REGULATIONS:

The Sheriff Should Have A Written Agreement To Protect Deposits

The Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. As of February 19, 2003, the date of the highest balance, the Sheriff had bank deposits at Inez Deposit Bank, PO Box 365, Inez, Kentucky of \$367,738; FDIC insurance of \$100,000; and collateral pledged or provided of \$1,143,500. As of March 14, 2003, the date of highest balance, the Sheriff had bank deposits at Family Bank, 232 Main Street, Paintsville, Kentucky of \$692,975; FDIC insurance of \$100,000; and collateral pledged or provided of \$1,088,000. Even though the Sheriff obtained sufficient collateral, there was no written agreement between the Sheriff and the depository institution, signed by both parties, securing the Sheriff's interest in the collateral. We recommend the Sheriff enter into a written agreement with the depository institution to secure the Sheriff's interest in the collateral pledged or provided by the depository institution. According to federal law, 12 U.S.C.A. § 1823(e), this agreement, in order to be recognized as valid by the FDIC, should be (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee and, (c) an official record of the depository institution.

Sheriff's Response:

I will comply.

The County Sheriff Should Not Transfer Money From The Fee Account To The Tax Account

Pursuant to KRS 134.170, other than for investments and expenditures permitted by KRS 134.140, the sheriff shall not apply or use any money received by him for any purpose other than that for which the money was paid or collected. The Sheriff transferred \$5,100 from the fee account to the tax settlement account. We recommend that in the future the sheriff comply with KRS 134.170. We also recommend the tax account repay the \$5,100 to the fee account.

Sheriff's Response:

I was not aware of this not being allowable. This will not happen in the future.

MARTIN COUNTY
GARMON PREECE, COUNTY SHERIFF
COMMENTS AND RECOMMENDATIONS
For The Period January 6, 2003 Through May 14, 2003
(Continued)

INTERNAL CONTROL - REPORTABLE CONDITIONS:

Lacks Adequate Segregation Of Duties

During our audit we noted the Sheriff's internal control structure lacked an adequate segregation of duties. This deficiency occurs when someone has custody over assets and the responsibility of recording financial transactions. In our judgment, this condition could adversely affect the Sheriff's ability to record, process, summarize, and report accurate financial information. We recommend the Sheriff obtain additional staff to divide the responsibilities or implement the following compensating controls that would help offset the lack of adequate segregation of duties:

- Cash recounted and deposited by the Sheriff
- Reconciliation of reports to source documents and receipts and disbursements ledgers by the Sheriff
- All disbursement checks are to be signed by two people and one must be the Sheriff
- The Sheriff examines payroll checks prepared by an employee and distributes checks to employees
- All disbursements checks prepared by an employee are examined by the Sheriff for proper documentation
- The Sheriff mails disbursements
- The Sheriff or someone independent of the Sheriff's Office prepares bank reconciliations

Sheriff's Response:

I will comply where I can.

PRIOR YEAR:

- The Sheriff Should Require Depository Institution To Pledge Or Provide Sufficient Collateral Of \$243,434 And Enter Into A Written Agreement To Protect Deposits

REPORT ON COMPLIANCE
AND ON INTERNAL CONTROL OVER FINANCIAL
REPORTING BASED ON AN AUDIT OF THE FINANCIAL STATEMENT
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Morgan-Franklin, LLC
P.O. Box 428
513 Main Street
West Liberty, Kentucky 41472

To the People of Kentucky

Honorable Paul E. Patton, Governor

Gordon C. Duke Secretary

Finance and Administration Cabinet

Dana Mayton, Secretary, Revenue Cabinet

Honorable Kelly Callahan, Martin County Judge/Executive

Honorable Garmon Preece, Martin County Sheriff

Members of the Martin County Fiscal Court

Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards

We have audited the Martin County Sheriff's Settlement - 2002 for the period January 6, 2003 through May 14, 2003, and have issued our report thereon dated October 6, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Martin County Sheriff's Settlement - 2002 Taxes for the period January 6, 2003 through May 14, 2003, is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under Government Auditing Standards and which are described in the accompanying comments and recommendations.

- The Sheriff Should Have A Written Agreement To Protect Deposits
- The County Sheriff Should Not Transfer Money From The Fee Account To The Tax Account

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Martin County Sheriff's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition.

Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of The Financial
Statements Performed In Accordance With Government Auditing Standards
(Continued)

Internal Control Over Financial Reporting (Continued)

Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statement. The reportable condition is described in the accompanying comments and recommendations.

- Lacks Adequate Segregation Of Duties

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we do not believe the reportable condition described above is a material weakness.

This report is intended solely for the information and use of management and is not intended to be and should not be used by anyone other than the specified party.

Respectfully submitted,

Morgan - Franklin, LLC

Morgan-Franklin, LLC

Audit fieldwork completed -
October 6, 2003

